

FINANCIAL REPORT

**TEXAS STATE UNIVERSITY –
SAN MARCOS
DEVELOPMENT FOUNDATION**

AUGUST 31, 2010 AND 2009

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Carneiro, Chumney & Co., L.C.

CERTIFIED PUBLIC ACCOUNTANTS

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

The Board of Trustees
Texas State University – San Marcos
Development Foundation
San Marcos, Texas

We have audited the Statements of Financial Position of Texas State University – San Marcos Development Foundation (the Foundation) as of August 31, 2010 and 2009, and the related Statements of Activities and Cash Flows for the years then ended. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with United States generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Foundation's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Texas State University – San Marcos Development Foundation as of August 31, 2010 and 2009, and the changes in its net assets and its cash flows for the years then ended, in conformity with United States generally accepted accounting principles.



March 8, 2011

TEXAS STATE UNIVERSITY - SAN MARCOS DEVELOPMENT FOUNDATION

STATEMENTS OF FINANCIAL POSITION

AUGUST 31, 2010 AND 2009

	2010	2009
ASSETS		
Assets:		
Cash	\$ 731,620	\$ 332,981
Investments:		
Marketable securities	38,208,161	34,343,537
Real estate	4,322	4,322
Pledges receivable - net	730,095	790,420
Prepaid expenses and other assets	8,056	56,636
Property and equipment - net	2,728	7,092
	<u>\$ 39,684,982</u>	<u>\$ 35,534,988</u>
LIABILITIES AND NET ASSETS		
Liabilities:		
Accounts payable	\$ 16,908	\$ 16,952
Annuities payable	522,013	521,358
	<u>538,921</u>	<u>538,310</u>
Net Assets:		
Unrestricted	180,203	155,581
Temporarily restricted	7,111,251	5,100,988
Permanently restricted	31,854,607	29,740,109
	<u>39,146,061</u>	<u>34,996,678</u>
	<u>\$ 39,684,982</u>	<u>\$ 35,534,988</u>

The accompanying notes are an integral part of these financial statements.

TEXAS STATE UNIVERSITY - SAN MARCOS DEVELOPMENT FOUNDATION

STATEMENT OF ACTIVITIES

YEAR ENDED AUGUST 31, 2010

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Support, Revenue, and Other:				
Contributions	\$ 1,328	277,741	2,122,375	\$ 2,401,444
Investment income	1,735	1,128,198	32,445	1,162,378
Realized and unrealized gains on marketable securities	1,036	1,467,424	72,933	1,541,393
Changes in split interests	--	8,046	(113,255)	(105,209)
Rent and royalties	--	10,920	--	10,920
Recovery of bad debt	5,825			5,825
Net Assets Released from Restrictions - Scholarships, university advancement, and management and general	882,066	(882,066)	--	--
Total Support, Revenue, and Other	891,990	2,010,263	2,114,498	5,016,751
Expenses:				
Program:				
Scholarships	336,368	--	--	336,368
University advancement	243,568	--	--	243,568
Supporting services	287,432	--	--	287,432
Total Expenses	867,368	--	--	867,368
Change in Net Assets	24,622	2,010,263	2,114,498	4,149,383
Net assets at beginning of year	155,581	5,100,988	29,740,109	34,996,678
NET ASSETS AT END OF YEAR	<u>\$ 180,203</u>	<u>7,111,251</u>	<u>31,854,607</u>	<u>\$ 39,146,061</u>

The accompanying notes are an integral part of these financial statements.

TEXAS STATE UNIVERSITY - SAN MARCOS DEVELOPMENT FOUNDATION

STATEMENT OF ACTIVITIES

YEAR ENDED AUGUST 31, 2009

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Support, Revenue, and Other:				
Contributions	\$ 452	235,300	2,784,574	\$ 3,020,326
Contributions - in-kind	3,600	--	--	3,600
Investment income	881	1,048,599	24,657	1,074,137
Realized and unrealized gains (losses) on marketable securities	1,779	(2,404,013)	(171,955)	(2,574,189)
Changes in split interests	--	(21,975)	(48,598)	(70,573)
Rent and royalties	--	14,360	--	14,360
Other income	--	303	--	303
Net Assets Released from Restrictions - Scholarships, University advancement, and management and general	1,613,808	(1,613,808)	--	--
Total Support, Revenue, and Other	1,620,520	(2,741,234)	2,588,678	1,467,964
Expenses:				
Program:				
Scholarships	694,862	--	--	694,862
University advancement	669,995	--	--	669,995
Supporting services	279,049	--	--	279,049
Total Expenses	1,643,906	--	--	1,643,906
Change in Net Assets	(23,386)	(2,741,234)	2,588,678	(175,942)
Net assets at beginning of year	178,967	7,842,222	27,151,431	35,172,620
NET ASSETS AT END OF YEAR	\$ 155,581	5,100,988	29,740,109	\$ 34,996,678

The accompanying notes are an integral part of these financial statements.

TEXAS STATE UNIVERSITY - SAN MARCOS DEVELOPMENT FOUNDATION

STATEMENTS OF CASH FLOWS

YEARS ENDED AUGUST 31, 2010 AND 2009

	2010	2009
Change in net assets	\$4,149,383	\$ (175,942)
Adjustments to Reconcile Change in Net Assets to Net Cash Provided by Operating Activities:		
Depreciation	4,364	4,364
Realized and unrealized (gains) losses on marketable securities	(1,541,393)	2,574,189
Fair value of land donated	(731,000)	--
Changes in split interests	105,209	70,573
Changes in Assets and Liabilities:		
Decrease in pledges receivable	60,325	217,002
Decrease in prepaid expenses and other assets	48,580	37,357
(Decrease) in accounts payable	(44)	(6,498)
Increase (decrease) in annuities payable	655	(18,678)
Net Cash Provided by Operating Activities	2,096,079	2,702,367
Cash Flows from Investing Activities:		
Purchase of marketable securities	(7,389,535)	(10,397,320)
Proceeds from sale of marketable securities	5,016,471	7,530,352
Proceeds from sale of land	731,000	--
Net Cash (Used in) Investing Activities	(1,642,064)	(2,866,968)
Cash Flows (Used in) Financing Activities -		
Payments on annuities	(55,376)	(60,099)
Net Increase (Decrease) in Cash	398,639	(224,700)
Cash at beginning of year	332,981	557,681
CASH AT END OF YEAR	\$ 731,620	\$ 332,981

The accompanying notes are an integral part of these financial statements.

TEXAS STATE UNIVERSITY – SAN MARCOS DEVELOPMENT FOUNDATION

NOTES TO FINANCIAL STATEMENTS

AUGUST 31, 2010 AND 2009

Note 1: Organization

Texas State University – San Marcos Development Foundation (the Foundation) (formerly Southwest Texas State University Development Foundation) is a nonprofit corporation formed to assist in the educational advancement of Texas State University – San Marcos (the University). The Foundation:

- invests and administers funds for the University's benefit;
- conducts development efforts for the benefit of the University, utilizing the expertise of those employees of the University who are assigned to work with the Foundation and the resources of the Foundation for that purpose;
- works with other groups which express an interest in assisting the University in pursuit of fundraising efforts;
- renders the same assistance to the University as it has rendered in the past and such additional assistance as may, in the future, appear mutually desirable, with changes that take place from time to time as agreed upon by the University and the Foundation, provided, however, that the Foundation's primary focus in the future will be on developing and maintaining long-term and short-term endowment monies; and
- recognizes the University as the sole beneficiary of its development policies and its educational support.

Note 2: Summary of Significant Accounting Policies

Basis of Accounting

The financial statements of the Foundation are prepared on the accrual basis of accounting, which follows United States generally accepted accounting principles (GAAP).

Basis of Reporting

The classes of net assets of the Foundation included in the accompanying financial statements are described below:

Unrestricted: Resources that are expendable at the discretion of the Foundation.

Temporarily Restricted: Resources whose use is restricted by donor-imposed stipulations that either expire by the passage of time or can be fulfilled and otherwise removed by actions of the Foundation pursuant to those stipulations.

Permanently Restricted: Resources whose use is restricted by donor-imposed stipulations that neither expire by the passage of time nor can be fulfilled or otherwise removed by actions of the Foundation.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

TEXAS STATE UNIVERSITY – SAN MARCOS DEVELOPMENT FOUNDATION

NOTES TO FINANCIAL STATEMENTS

AUGUST 31, 2010 AND 2009

Note 2: Summary of Significant Accounting Policies (Continued)

Fair Value of Financial Instruments

The Fair Value Measurements and Disclosures Topic of the FASB ASC, 820-10, defines fair value, establishes a three-level valuation hierarchy for disclosure of fair value measurements, and expands disclosures about fair value measurements. An instrument's categorization within the hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

Level 1 – Inputs that utilize quoted prices (unadjusted) in active markets for identical assets that the Foundation has the ability to access.

Level 2 – Inputs that include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. Fair values for these instruments are estimated using pricing models, quoted prices of securities with similar characteristics, or discounted cash flows.

Level 3 – Inputs that are unobservable inputs for the asset or liability, which are typically based on an entity's own assumptions, as there is little, if any, related market activity.

Cash

Cash held in the trust account by brokers is considered an investment rather than cash or cash equivalent.

Investments and Investment Income

Investments are principally comprised of publicly traded mutual funds that invest in equity and debt securities. Fair market trade value is based on the last sale price on the last business day of the year, or on the most current traded date subsequent to year end. As required by the Fair Value Measurements Topic of the FASB Accounting Standards Codification, the Foundation reports investments in equity securities with readily determinable fair values, and all investments in debt securities, at fair value with gains and losses included, in the Statement of Activities.

The majority of investments are pooled for the purpose of maximizing income. Income consists of investment income (interest and dividends) as well as realized and unrealized gains and/or losses. Revenue and gains are allocated based on the principal of individual accounts. These investments are maintained by a registered dealer and are managed by an investment manager (see Note 4).

Unrestricted investment income is recognized as revenue and gains when earned. Unrestricted investment income includes income from net assets where no restriction has been placed by the donor on its use. Investment income that is temporarily or permanently restricted by the donor is reclassified to unrestricted net assets, when the donor imposed stipulations are fulfilled.

Pledges and Contributions

The Foundation recognizes promises to give (pledges) in the financial statements when there is sufficient evidence in the form of verifiable documentation that a promise was made. Unconditional promises to give that are expected to be collected within one year are recorded at net realizable value. Conditional promises (such as matching grants) to give are not included as support until the conditions are substantially met.

TEXAS STATE UNIVERSITY – SAN MARCOS DEVELOPMENT FOUNDATION

NOTES TO FINANCIAL STATEMENTS

AUGUST 31, 2010 AND 2009

Note 2: Summary of Significant Accounting Policies (Continued)

Pledges and Contributions (Continued)

Contributed real estate is recorded at fair value at the date of donation. Real estate is reported at its original fair value until sold. The Foundation records contributed property and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. If a donor stipulates how long the assets must be used, the contribution is recorded as temporarily restricted support.

All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are designated for future periods, or restricted by the donor for specific purposes, are reported as temporarily restricted or permanently restricted support that increases those net asset classes. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statement of Activities as net assets released from restrictions.

The Foundation entered into an agreement with the University to use its administration and employees to provide reasonable and necessary support to the Foundation. These contributed services and supplies are recognized as income and expense if they (a) create or enhance nonfinancial assets, or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not contributed. These services are recognized at the fair value and included in the Statement of Activities (see Note 8).

Bad Debt Expense

The Foundation uses the direct write-off method to record bad debts. This method is not considered to be materially different from the allowance method as required under GAAP.

Property and Equipment

Purchased equipment is recorded at historical cost. Depreciation of equipment is calculated on the straight-line basis based on estimated useful lives of five years.

Annuities Payable and Split Interest Agreements

The Foundation has entered into several Charitable Gift Annuity Agreements whereby the donor contributes assets in exchange for distributions based on the value of trust assets for a specified period of time. These are amounts estimated by management for future payments to donor designated beneficiaries. On an annual basis, the Foundation revalues the liability based on applicable mortality tables and discount rates varying currently at approximately 6%.

Federal Income Taxes

The Foundation is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. However, the Foundation is subject to taxation on the net income, if any, derived from activities that are not considered to be related to the operations for which the Foundation's tax exemption was granted. The Foundation adopted the provisions of FASB ASC topic 740-10-25, *Income Taxes – Overall – Recognition*, which requires recognition and disclosure of uncertain tax positions in the financial statements and footnotes. Management of the Foundation believes that it has appropriate support for any tax positions taken and, as such, does not have any uncertain tax positions that are material to the financial statements.

TEXAS STATE UNIVERSITY – SAN MARCOS DEVELOPMENT FOUNDATION

NOTES TO FINANCIAL STATEMENTS

AUGUST 31, 2010 AND 2009

Note 3: Concentration of Credit Risk

Financial instruments which potentially subject the Foundation to a concentration of credit risk consist principally of cash. The Foundation maintains bank accounts at a single financial institution in San Marcos, Texas. Accounts at this institution are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 for interest-bearing accounts, and without limit for noninterest-bearing transaction accounts. At various times during the year there were balances in the bank that were over the FDIC limit. Subsequent to year end, the interest-bearing sweep was eliminated and all monies are currently fully covered in a noninterest-bearing account.

Note 4: Investments

The cost and fair value of investments in marketable securities at August 31 were as follows:

	<u>2010</u>		<u>2009</u>	
	<u>Cost</u>	<u>Fair Value</u>	<u>Cost</u>	<u>Fair Value</u>
Money market accounts	\$ 435,937	435,937	427,073	\$ 427,073
Corporate bonds	--	--	123,357	65,560
Equity securities	1,500,000	355,772	1,500,000	516,054
Mutual funds	35,397,982	35,781,140	33,688,322	31,898,623
Stocks	9,580	10,290	--	--
Other assets	<u>1,525,957</u>	<u>1,625,022</u>	<u>1,413,267</u>	<u>1,436,227</u>
Total	\$ <u>38,869,456</u>	<u>38,208,161</u>	<u>37,152,019</u>	\$ <u>34,343,537</u>

Note 5: Pledges Receivable

As required by the Fair Value Measurements Topic of the FASB, ASC 820-10, the recorded pledges have been discounted to their present value using a discount rate of 5%. Pledges receivable at August 31 consisted of the following:

	<u>2010</u>	<u>2009</u>
Pledges permanently restricted	\$ 783,235	\$ 850,338
Less: Unamortized discount	<u>(53,140)</u>	<u>(59,918)</u>
Pledges Receivable – Net	\$ <u>730,095</u>	\$ <u>790,420</u>
Amount Due in:		
Less than one year	\$ 232,135	\$ 249,385
One to five years - net	469,044	512,119
Over five years - net	<u>28,916</u>	<u>28,916</u>
	\$ <u>730,095</u>	\$ <u>790,420</u>

Note 6: Property and Equipment

Property and equipment at August 31 were as follows:

	<u>2010</u>	<u>2009</u>
Computer equipment and software	\$ 21,822	\$ 21,822
Less: Accumulated depreciation	<u>(19,094)</u>	<u>(14,730)</u>
Net Property and Equipment	\$ <u>2,728</u>	\$ <u>7,092</u>

TEXAS STATE UNIVERSITY – SAN MARCOS DEVELOPMENT FOUNDATION

NOTES TO FINANCIAL STATEMENTS

AUGUST 31, 2010 AND 2009

Note 7: Net Asset Receivable/Payable (Unaudited)

Temporarily restricted net assets are comprised of individual funds, some of which have over-expended balances and some of which have under-expended balances. Management is aware that amounts are owed between funds and will make future expenses in accordance with the nature and amounts available. Total individual funds for 2010 and 2009 were over-expended by \$66,788 and \$341,803, respectively, of earnings; total individual funds available to spend as of August 31, 2010 and 2009 were \$7,181,067 and \$4,807,952, respectively.

Note 8: In-Kind Contributions

The Foundation recognizes in-kind contributions for certain eligible expenses at the fair value of those expenses. In-kind contributions totaled \$0 and \$3,600 for the fiscal 2010 and 2009 years, respectively, and have been included in contributions and management and general expenses in the Statements of Activities. These services included office rent, telephone, and utilities (see Note 10).

Note 9: Schedule of Conditional Future Income

The Foundation is the named beneficiary of various wills and life insurance policies. Receipt of the related assets is conditional in that the future payment cannot be legally enforced, and so they are not recorded as assets. As of August 31, 2010, the cash surrender value of the life insurance policies was \$772,615 (unaudited). In the case of the wills and the proceeds from life insurance policies, discounted values of the future collections under the instruments are calculated from actuarial tables, based on the donor's life expectancy. Detailed records and relevant documents in connection with these accounts are maintained by the Texas State University Advancement Department and the Development Foundation.

Total conditional future income as of August 31, 2010 consists of:

<u>Source</u>	<u>Face Value</u>	<u>Discounted Value</u>
Wills	\$ 14,185,000	\$ 10,573,557
Life insurance policies	<u>3,383,531</u>	<u>896,869</u>
Total Conditional Future Income	\$ <u>17,568,531</u>	\$ <u>11,470,426</u>

TEXAS STATE UNIVERSITY – SAN MARCOS DEVELOPMENT FOUNDATION

NOTES TO FINANCIAL STATEMENTS

AUGUST 31, 2010 AND 2009

Note 10: Schedule of Expenses - Supporting Services

	<u>2010</u>			<u>2009</u>		
	<u>Amount</u>	<u>In-Kind</u>	<u>Total</u>	<u>Amount</u>	<u>In-Kind</u>	<u>Total</u>
	<u>Paid</u>	<u>(Note 8)</u>		<u>Paid</u>	<u>(Note 8)</u>	
Supporting Services:						
Management and General:						
Allocated services	\$ 127,065	--	127,065	121,220	--	\$ 121,220
Depreciation expense	4,364	--	4,364	4,364	--	4,364
Equipment	3,326	--	3,326	3,445	--	3,445
Insurance	22,373	--	22,373	27,255	--	27,255
Investment and banking fees	95,421	--	95,421	85,427	--	85,427
Legal and professional	22,836	--	22,836	20,200	--	20,200
Office printing and supplies	1,128	--	1,128	1,961	--	1,961
Office rent	--	--	--	--	2,400	2,400
Postage	10	--	10	643	--	643
Tax	--	--	--	76	--	76
Telephone	--	--	--	--	600	600
Utilities	--	--	--	--	600	600
Total Management and General	276,523	--	276,523	264,591	3,600	268,191
Fundraising –						
Travel and entertainment	<u>10,909</u>	<u>--</u>	<u>10,909</u>	<u>10,858</u>	<u>--</u>	<u>10,858</u>
Total Fundraising	<u>10,909</u>	<u>--</u>	<u>10,909</u>	<u>10,858</u>	<u>--</u>	<u>10,858</u>
Total Supporting Services	\$ <u>287,432</u>	<u>--</u>	<u>287,432</u>	<u>275,449</u>	<u>3,600</u>	\$ <u>279,049</u>

Note 11: Fair Values of Financial Instruments

The reporting entity uses fair value measurements to record fair value adjustments to certain assets and liabilities to determine fair value disclosures. For additional information on how the Foundation measures fair value, refer to Note 2: Summary of Significant Accounting Policies.

The following description of the valuation methods and assumptions were used by the Foundation in estimating the fair value disclosures for financial assets. There have been no changes in methodologies used at August 31, 2010 and 2009:

Corporate Bonds, Money Market and Mutual Funds, and Exchange-Traded Funds – Valued at the fair value of shares at quoted market prices held by the Foundation at fiscal year end.

TEXAS STATE UNIVERSITY – SAN MARCOS DEVELOPMENT FOUNDATION

NOTES TO FINANCIAL STATEMENTS

AUGUST 31, 2010 AND 2009

Note 11: Fair Values of Financial Instruments (Continued)

Equity Securities – Valued at the prorated fair value of shares for a partial quarter, held by the Foundation at fiscal year end.

Stocks – Valued at the fair value of shares at quoted market prices held by the Foundation at fiscal year end, for assets traded regularly.

Promises to Give – Valued at the discounted present value of the long-term promises to give.

Annuities Payable – Valued at the estimated present value of the annuitant obligation using discount rates provided by IRS guidelines.

The following tables set forth by level, within the fair value hierarchy, the Foundation's assets and liabilities at fair value as of August 31:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
2010:				
Money markets	\$ 435,937	--	--	\$ 435,937
Equity securities	--	--	355,772	355,772
Mutual funds	35,781,141	--	--	35,781,141
Exchange-traded funds	--	1,582,369	--	1,582,369
Stocks	52,942	--	--	52,942
Promises to give	--	--	730,095	730,095
Annuities payable	--	--	522,013	522,013
Total Assets and Liabilities at Fair Value	<u>\$ 36,270,020</u>	<u>1,582,369</u>	<u>1,607,880</u>	<u>\$ 39,460,269</u>
2009:				
Money markets	\$ 427,073	--	--	\$ 427,073
Corporate bonds	65,560	--	--	65,560
Equity securities	--	--	516,054	516,054
Mutual funds	31,898,623	--	--	31,898,623
Exchange-traded funds	--	1,393,574	--	1,393,574
Stocks	42,653	--	--	42,653
Promises to give	--	--	790,420	790,420
Annuities payable	--	--	521,358	521,358
Total Assets and Liabilities at Fair Value	<u>\$ 32,433,909</u>	<u>1,393,574</u>	<u>1,827,832</u>	<u>\$ 35,655,315</u>

TEXAS STATE UNIVERSITY – SAN MARCOS DEVELOPMENT FOUNDATION

NOTES TO FINANCIAL STATEMENTS

AUGUST 31, 2010 AND 2009

Note 11: Fair Values of Financial Instruments (Continued)

Level 3 Gains and Losses

The following tables set forth a summary of changes in the fair value of the Foundation's Level 3 assets for the year ended August 31, 2010:

Equity Securities:	
Balance, beginning of year	\$ 516,054
Unrealized (losses)	<u>(160,282)</u>
Balance, End of Year	\$ <u>355,772</u>
 Promises to Give:	
Balance, beginning of year	\$ 790,420
New pledges	95,603
Payments on pledges	(149,150)
Change in discount	<u>(6,778)</u>
Balance, End of Year	\$ <u>730,095</u>
 Annuities Payable:	
Balance, beginning of year	\$ 521,358
Payments to annuitants	(55,376)
Change in split interests affecting annuities payable	<u>56,031</u>
Balance, End of Year	\$ <u>522,013</u>

Note 12: Endowment Funds

General Information

The Foundation maintains various endowment funds established for a variety of purposes. These endowments include both donor-restricted endowment contributions, and funds designated by the Board of Trustees to function as endowments. The donor-restricted endowment funds fall under the provisions of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA), which was adopted by the state of Texas, with an effective date of September 1, 2007. This policy defines the Foundation's interpretation of the provisions of this law as it relates to the prudent management of its endowment fund.

Background

In July, 2006, the Uniform Law Commission (ULC) approved UPMIFA as a modernized version of the Uniform Management of Institutional Funds Act of 1972 (UMIFA) which governed the investment and management of donor-restricted endowment funds by not-for-profit organizations. The major change of the new law is that UPMIFA prescribes new guidelines for expenditure of a donor-restricted endowment fund when there are no explicit donor stipulations. These guidelines require the Foundation to determine what constitutes prudent spending based upon consideration of the donor's intent that the endowment fund continues permanently, the purpose of the fund, and relevant economic factors. UPMIFA emphasizes the perpetuation of the purchasing power of the fund, not just the original dollars contributed to the fund. Although the Act does not require that a specified amount be set aside as principal, the Act assumes that an organization will preserve "principal" by maintaining the purchasing power of amounts contributed, and will spend "income" by making distributions using a reasonable spending rate.

TEXAS STATE UNIVERSITY – SAN MARCOS DEVELOPMENT FOUNDATION

NOTES TO FINANCIAL STATEMENTS

AUGUST 31, 2010 AND 2009

Note 12: Endowment Funds (Continued)

Endowment "Principal" Interpretation

The Foundation has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds, absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment (the Principal). The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets, is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Foundation in a manner consistent with the standard of prudence prescribed by UPMIFA.

Endowment Investment Objectives

Endowment investments are managed by professional money manager(s) under the direction of the Business Affairs Committee of the Board of Trustees of the Foundation. Funds are invested in a manner that seeks to produce results that meet or exceed the performance of generally recognized market indices, while assuming a moderate level of investment risk.

To satisfy this performance objective, the Foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Foundation targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives, within prudent risk constraints.

Endowment "Income" Appropriation (Spending Policy)

The Foundation's policy is to appropriate for distribution each year a percentage of each endowment fund based on a rate determined by the audit committee annually. For fiscal years ended 2010 and 2009, the percentage was 3%, respectively. In establishing this policy, the Foundation considered the long-term expected return on its endowment. Accordingly, over the long term, the Foundation expects the spending policy to allow its endowment to grow at an average of 4% annually. This is consistent with the Foundation's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term, as well as provide additional real growth through new gifts and investment return.

In accordance with UPMIFA, in all its endowment spending activity, the Foundation considers the following factors in making a determination to appropriate (spend) or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund
2. The purposes of the Foundation and the donor-restricted endowment fund
3. General economic and investment market conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of the Foundation, and
7. The investment policies of the Foundation

TEXAS STATE UNIVERSITY – SAN MARCOS DEVELOPMENT FOUNDATION

NOTES TO FINANCIAL STATEMENTS

AUGUST 31, 2010 AND 2009

Note 12: Endowment Funds (Continued)

Total Net Asset Composition by Type of Fund as of August 31, 2010

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ --	7,111,251	31,854,607	\$ 38,965,858
Undesignated	<u>180,203</u>	<u>--</u>	<u>--</u>	<u>180,203</u>
Total Funds	\$ <u>180,203</u>	<u>7,111,251</u>	<u>31,854,607</u>	\$ <u>39,146,061</u>

Changes in Endowment Net Assets for the Year Ended August 31, 2010 (All Donor Restricted Endowment Funds)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ --	5,100,988	29,740,109	\$ 34,841,097
Investment Return:				
Investment income	--	1,139,119	32,445	1,171,564
Net gains (losses) (realized and unrealized)	<u>--</u>	<u>1,475,469</u>	<u>(40,322)</u>	<u>1,435,147</u>
Total Investment Return	--	2,614,588	(7,877)	2,606,711
Contributions	--	277,741	2,122,375	2,400,116
Appropriations of endowment net assets for expenditure	<u>--</u>	<u>(882,066)</u>	<u>--</u>	<u>(882,066)</u>
Endowment Net Assets, End of Year	\$ <u>--</u>	<u>7,111,251</u>	<u>31,854,607</u>	\$ <u>38,965,858</u>

Total Net Asset Composition by Type of Fund as of August 31, 2009

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ --	5,100,988	29,740,109	\$ 34,841,097
Undesignated	<u>155,581</u>	<u>--</u>	<u>--</u>	<u>155,581</u>
Total Funds	\$ <u>155,581</u>	<u>5,100,988</u>	<u>29,740,109</u>	\$ <u>34,996,678</u>

TEXAS STATE UNIVERSITY – SAN MARCOS DEVELOPMENT FOUNDATION

NOTES TO FINANCIAL STATEMENTS

AUGUST 31, 2010 AND 2009

Note 12: Endowment Funds (Continued)

Changes in Endowment Net Assets for the Year Ended August 31, 2009 (All Donor Restricted Endowment Funds)

	<u>Unrestricted</u>	Temporarily <u>Restricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ --	7,842,222	27,151,431	\$ 34,993,653
Investment Return:				
Investment income	--	1,062,959	24,657	1,087,616
Net losses (realized and unrealized)	<u>--</u>	<u>(2,425,988)</u>	<u>(220,553)</u>	<u>(2,646,541)</u>
Total Investment Return	--	(1,363,029)	(195,896)	(1,558,925)
Contributions	--	235,300	2,784,574	3,019,874
Appropriations of endowment net assets for expenditure	--	(1,613,808)	--	(1,613,808)
Other changes	<u>--</u>	<u>303</u>	<u>--</u>	<u>303</u>
Endowment Net Assets, End of Year	\$ <u>--</u>	<u>5,100,988</u>	<u>29,740,109</u>	\$ <u>34,841,097</u>

Note 13: Inherited Property

The Foundation received two donations of real property during the year. One property was ranchland in the Smithville area. The land was appraised, but sold shortly after the transfer. The actual sales price of \$731,853 was less than the appraised amount of \$936,000. The Foundation recorded the lesser of the two as the donated amount, due to management's belief that the selling price represented a more accurate fair market value. The other property was a house in Smithville, which is to be used as part of a writer-in-residence program. The Foundation does not manage any other property and since the University will administer the program, the house was transferred to Texas State University-San Marcos. The house was appraised at \$130,000. The Foundation recorded the transfer of the house to Texas State University-San Marcos as University support.

Note 14: Subsequent Events

Subsequent events have been evaluated through the date of this report, which is the date the financial statements were available to be issued.